



United States
General Accounting Office
Washington, D.C. 20548

Accounting and Information
Management Division

B-277089

July 21, 1997

The Honorable Charles E. Grassley
United States Senate

Subject: Financial Management: DOD Progress Payment Distribution
Procedures

Dear Senator Grassley:

The Department of Defense (DOD) has long recognized that distributing and accounting for contract progress payments are major contributors to its problems in accurately accounting for disbursements. Over the past several years, a number of different methods have been used within the Department to distribute and account for progress payments when more than one appropriation is used to fund a contract. A distribution method is necessary because contractors are not required to identify the funding appropriations when submitting progress payment requests.

On April 22, 1997, we briefed your office on selected DOD progress payment accounting methods which are being used, or have been used over the past several years, to distribute progress payments. Subsequent to the briefing, your office requested an illustration of the differences between and results of each of the progress payment accounting methods discussed during the briefing.

Defense Finance and Accounting Service (DFAS) officials have stated that the DOD Financial Management Regulation 7000.14R, Volume 10, Contract Payment Policy and Procedures, issued in February 1996, provides the only currently sanctioned DOD policy governing progress payment distribution. It provides standard progress payment accounting policies for distributing progress payments and requires DFAS centers to issue additional guidance prescribing detailed implementing procedures.

CURRENT DISTRIBUTION METHODS TO ACCOUNT
FOR PROGRESS PAYMENTS

DFAS officials stated that the DOD Financial Management Regulation 7000.14R, Volume 10, defines two basic methods for distributing progress payments:

(1) specific instructions as requested and directed in a contract and (2) proration using obligation balances as the basis (commonly referred to as the Automatic Payment of Invoices (API) method). In addition, according to the officials, an October 3, 1995, policy memorandum issued by DFAS-Columbus is to be followed when payments are rejected for automatic allocation and staff have to resort to manually allocating progress payments among the funding appropriations. This represents a third method. Selected details on each of these distribution methods follow.

- Contract specific payment instructions require progress payments to be distributed in accordance with instructions provided by individual contracts.
- The Mechanization of Contract Administration Services (MOCAS) API procedure establishes a payment distribution procedure based on the weighted value of the contract's total obligations. This procedure was implemented in 1982 and adopted by DFAS-Columbus as part of the consolidation of DOD's finance and accounting functions. The API method is used today for approximately 80 percent of the progress payments processed by DFAS-Columbus.
- DFAS-Columbus October 3, 1995, policy memorandum prescribes manual progress payment distribution processes that allocate payments in alphabetic order based on accounting classification reference numbers¹ (ACRN). This memorandum establishes DFAS-Columbus payment distribution procedures consistent with the DOD Comptroller's September 28, 1995, directive.² While not a prorated distribution as required by Volume 10 of the Financial Management Regulation, DFAS officials have stated the overall policy prescribed in Volume 10 is supplemented by the October 3, 1995, policy memorandum which allows an expedient, but less precise allocation method, in order to facilitate timely payments to contractors.

Finally, our work in the disbursement area has identified other accounting methods used by DFAS-Columbus personnel to distribute progress payments.

¹ACRNs are a two-character code assigned to each unique accounting line in a contract. DOD uses accounting lines to accumulate appropriation, budget, and management information for contract obligations and payments.

²On September 28, 1995, the DOD Comptroller issued a memorandum directing a change to DFAS's progress payment allocation method. The change required that DFAS initially attempt to allocate progress payments to all contract ACRN's on a prorata basis using total contract obligations. If prevalidation processes rejected the payment, the change mandated a manual allocation in "ACRN sequence based on the progress payment rate."

One such method is exemplified in enclosure V. In addition, when recording the payment transaction in the official accounting records, accounting station personnel have used other methods, which may change the original distribution made by DFAS-Columbus.³

OTHER PAYMENT DISTRIBUTION METHODS

In addition to the four methods discussed above, your office also asked us to demonstrate the results of applying the following two progress payment distribution methods which have also been used.

- Air Force Regulation 177-120, Accounting and Finance Central Procurement Transactions,⁴ requires distribution to the oldest fiscal year funds first. Although not specifically noted as superseded in the Financial Management Regulation, DFAS officials told us that Air Force Regulation 177-120 was superseded by the Financial Management Regulation and is no longer to be used as guidance in distributing and accounting for progress payments.

- DFAS-Columbus Desk Procedure 302, Manual Distribution, was finalized on March 16, 1992, and applied the same methodology as the API procedures described above for those progress payments rejected from the automated process. A September 28, 1995, DOD Comptroller memorandum directed this policy to be discontinued because it created an excessive number of prevalidation requests and disrupted payments.

³In December 1993, we reported that for fiscal year 1992, 17 percent of the Army's disbursements made by offices other than the Army office responsible for controlling the funds were charged to a different appropriation when the responsible funding organizations matched them to the obligations (GAO/AIMD-94-12, December 22, 1993). We have not reviewed Air Force or Navy disbursements to determine if similar accounting practices exist, nor have we updated the Army information since the completion of the fiscal year 1992 review.

⁴The Army and Navy also had separate regulations governing progress payment accounting on their respective contracts. Information on these regulations is not provided since your staff specifically requested details on the method prescribed under Air Force Regulation 177-120.

APPLICATION OF PAYMENT DISTRIBUTION METHODS

Table I summarizes the effect of applying each of the above-mentioned progress payment distribution methods to the same progress payment request of \$1,525,000. Even though for one of the methods illustrated we applied an Air Force method to the Army progress payment request, the illustrations aptly demonstrate the payment distribution differences resulting from the use of various progress payment accounting methods. The amount distributed to the two appropriations⁵ varied from nothing to the entire payment, depending on the method used.

Table 1: Progress Payment Distribution Using Various DOD and Military Service Regulations and Procedures

Method	Fiscal Year 1995 Other Procurement, Army	Fiscal Year 1994 Other Procurement, Army
FMR methods		
<i>Current methods:</i>		
Contract specific instructions	a	a
API	\$782,736.75	\$742,263.25
<i>Supplemental instructions:</i>		
DFAS-Columbus 10/3/95 memo	\$1,525,000.00	\$0.00
<i>Other obligation based methods:</i>		
Other obligation based prorations ^b	\$782,782.50	\$742,217.50
Other methods		
Air Force regulation	\$0.00	\$1,525,000.00
DFAS-Columbus desk procedure	\$782,736.75	\$742,263.25

^aThe progress payment dollar amount distributed to each appropriation would vary based upon the specific amounts stated in the contract or the payment request.

^bThe dollar difference between the API method and the other obligation-based method will increase as more deliveries occur under the contract, resulting in a decrease in the unliquidated obligation balances.

Source: GAO analysis based on DOD policies and regulations

⁵The request selected pertains to a contract involving only two ACRNS and was selected for illustrative purposes only. Contracts involving 10 or more ACRNs account for 77 percent of the dollar value of DFAS-Columbus contracts.

Our work was performed in accordance with generally accepted government auditing standards between March 1997 and May 1997. Our scope and methodology is in enclosure I. Enclosure II provides more detailed information on progress payment requirements and other contract information pertinent to illustrating the results of the progress payment distribution methods. Enclosures III through VII illustrate the payment distribution results of applying five of the six methodologies. The sixth method, contract specific payment instructions, is not illustrated because the amount applied to contract ACRNs would be determined based upon unique information provided on a payment request.

AGENCY COMMENTS AND OUR EVALUATION

In written comments on a draft of this letter (see enclosure VIII), DOD stated that DFAS-Columbus has one policy governing the distribution of progress payments, supplemented by a policy memorandum that is used when payments are rejected from the MOCAS API process. DOD stated that this policy allows two distribution methods: (1) specific distribution as directed in the contract or (2) proration using obligation balances, which it refers to as API. Our work has shown that distribution methods, other than the two described by DOD, such as the one described in enclosure V, have also been used by DOD since DOD regulation 7000.14R Financial Management Regulation, Volume 10, was issued.

The Comptroller stated that he will soon require contracting officers or contract administration officers to provide DFAS with specific progress payment distribution instructions on all new contracts. The distributions are to reflect the contract line item level costs incurred by the contractor. However, it should be noted that because existing contracts authorizing the use of progress payments are generally long-term in nature, we believe it is likely to be a number of years before such a policy applied to new contracts will be a predominant progress payment distribution method.

We are sending copies of this letter to the Chairmen and Ranking Minority Member of the Senate Committee on Armed Services, the House Committee on National Security, the Senate Committee on Governmental Affairs, the House Committee on Government Reform and Oversight, the House Subcommittee on Government Management, Information, and Technology, the Senate Committee on Appropriations, and the House Committee on Appropriations. We are also sending copies of this letter to the Director of the Office of Management and Budget, the Under Secretary of Defense, Comptroller, the Director, Defense Finance and Accounting Service, and other interested parties. Copies will be made available to others upon request. If you or your staff have any questions or we can be of further assistance, please contact me at (202) 512-9095.

Sincerely yours,



Lisa G. Jacobson
Director, Defense Audits

Enclosures

SCOPE AND METHODOLOGY

To illustrate the differing results obtained when applying the six progress payment distribution methodologies discussed in the letter, we used the same actual progress payment request. An actual payment request processed by DFAS-Columbus was selected. The request, for \$1,525,000, pertained to an Army contract including two ACRNs representing two different appropriations--Fiscal Year 1994 Other Procurement, Army, and Fiscal Year 1995 Other Procurement, Army. We did not audit the validity of the progress payment request.

We did not illustrate all progress payment distribution methodologies which DOD is using, or has used, over the past several years. Instead, we illustrated only selected methodologies used since the issuance of the DOD Inspector General's report on the Titan IV program.¹ For example, we have not illustrated Army and Navy regulations governing progress payment accounting.

We performed our work from March 1997 through May 1997 in accordance with generally accepted government auditing standards. DOD provided written comments on a draft of this letter. These comments are presented and evaluated in the "Agency Comments and Our Evaluation" section and are reprinted in enclosure VIII.

¹Titan IV Program (DOD Inspector General report 92-064, March 31, 1992).

CONTRACT INFORMATION APPLICABLE TO EACH METHOD OF DISTRIBUTING
PROGRESS PAYMENTS

The following information is applicable to all distribution illustrations.

Table II.1: Contract ACRNs and Balances Per MOCAS

ACRN	Obligation Balance	Work-in-process balance	Unliquidated obligation balance
AA ^a	\$14,652,354.07	\$2,721,585.58	\$8,470,314.19
AB ^b	13,894,788.00	4,267,197.54	10,280,188.00

^aACRN AA represents FY 1995 Other Procurement, Army Appropriation.

^bACRN AB represents FY 1994 Other Procurement, Army Appropriation.

Source: GAO analysis based on DOD data.

Seventy-five percent of the amount of each requested progress payment is actually paid.

The approved progress payment of \$1,525,000.00 to be processed under this contract is the 10th request received. No specific payment distribution instructions have been provided. (See figure II.1.)

Figure II.1: Progress Payment Request

6. RATES		7. DATE OF INITIAL AWARD		5. CONTRACT PRICE \$ 28,547,142	
a. PROG PAY	75%	YEAR	MONTH	8. a. PROGRESS PAYMENT NO.	10
b. LIQUIDATE	75%	1995	AUG	b. DATE OF REQUEST	04/11/97
SECTION #2 STATEMENT OF COST UNDER THIS CONTRACT THROUGH					04/05/97
9. PAID COSTS ELIGIBLE UNDER PROGRESS PAYMENT CLAUSE					3,090,939
10. INCURRED COSTS ELIGIBLE UNDER PROGRESS PAYMENT CLAUSE					14,472,816
11. TOTAL COSTS ELIGIBLE FOR PROGRESS PAYMENTS (ITEM 9 + 10)					17,563,755
12. a. TOTAL COSTS INCURRED TO DATE					18,722,867
b. ESTIMATED ADDITIONAL COST TO COMPLETE					9,377,128
13. ITEM 11 MULTIPLIED BY ITEM 6a					13,172,816
14. a. PROGRESS PAYMENTS PAID TO SUBCONTRACTORS					6,105,634
b. LIQUIDATED PROGRESS PAYMENTS TO SUBCONTRACTORS					3,417,187
c. UNLIQUIDATED PROGRESS PAYMENTS TO SUBCONTRACTORS (ITEM 14c - 14b)					2,688,447
d. SUBCONTRACT PROGRESS PAYMENTS APPROVED FOR CURRENT PAYMENT					
e. ELIGIBLE SUBCONTRACTOR PROGRESS PAYMENTS (ITEM 14c + 14d)					2,688,447
15. TOTAL DOLLAR AMOUNT					15,861,263
16. ITEM 5 MULTIPLIED BY ITEM 6b					21,410,357
17. LESSOR OF ITEM 15 OR ITEM 16					15,861,263
18. TOTAL AMOUNT OF PREVIOUS PROGRESS PAYMENTS REQUESTED					14,336,263
19. MAXIMUM BALANCE ELIGIBLE FOR PROGRESS PAYMENTS (ITEM 17 - 18)					1,525,000
SECTION #3 COMPUTATION OF LIMITS FOR OUTSTANDING PROGRESS PAYMENTS					
20. COMPUTATION OF PROGRESS PAYMENT CLAUSE LIMITATION:					
a. COSTS INCLUDED IN ITEM 11 APPLICABLE TO ITEMS DELIVERED, INVOICED, AND ACCEPTED TO THE DATE IN HEADING OF SECTION #2.					10,927,046
b. COSTS ELIGIBLE FOR PROGRESS PAYMENTS, APPLICABLE TO UNDELIVERED ITEMS AND TO DELIVERED ITEMS NOT INVOICED AND ACCEPTED (ITEM 11 less 20a).					6,636,709
c. ITEM 20b MULTIPLIED BY ITEM 6a					4,977,532
d. ELIGIBLE SUBCONTRACTOR PROGRESS PAYMENTS (ITEM 14e)					2,688,447
e. LIMITATION (ITEM 20c + 20d)					7,665,979
21. COMPUTATION OF PROGRESS PAYMENT CLAUSE LIMITATION:					
a. CONTRACT PRICE OF ITEMS DELIVERED, ACCEPTED AND INVOICED TO DATE IN HEADING OF SECTION #2.					11,100,925
b. CONTRACT PRICE OF ITEMS NOT DELIVERED, ACCEPTED AND INVOICED (ITEM 5 less 21a).					17,446,217
c. ITEM 21b MULTIPLIED BY ITEM 6b					13,084,663
d. UNLIQUIDATED ADVANCE PAYMENTS PLUS ACCRUED INTEREST					
e. LIMITATION (ITEM 21c less 21d)					13,084,663
22. MAXIMUM UNLIQUIDATED PROGRESS PAYMENTS (LESSER OF ITEM 20e OR 21e)					7,665,979
23. TOTAL AMOUNT APPLIED & TO BE APPLIED TO REDUCE PROGRESS PAYMENTS					8,325,694
24. UNLIQUIDATED PROGRESS PAYMENTS (ITEM 18 less 23)					6,010,569
25. MAXIMUM PERMISSIBLE PROGRESS PAYMENTS (ITEM 22 less 24)					1,655,410
26. AMOUNT OF CURRENT INVOICE FOR PROGRESS PAYMENT (LESSER OF ITEM 25 OR 19)					1,525,000
27. AMOUNT APPROVED BY CONTRACTING OFFICER					

CERTIFICATION

I certify that the above statement (with attachments) has been prepared from the books and records of the above-named contractor in accordance with the contract and the instructions hereon, and to the best of my knowledge and belief, that it is correct that all the costs of contract performance (except as herewith reported in writing) have been paid to the extent shown herein, or where not shown as paid have been paid or will be paid currently by the contractor when due, in the ordinary course of business, that the work reflected above has been performed, that the quantities and amounts involved are consistent with the requirements of the contract. That there are no encumbrances (except as reported in writing herewith, or on previous progress payment request No. _____) against the property acquired or produced for, and allocated or properly chargeable to the contract which would affect or impair the Government's title, that there has been no materially adverse change in the financial condition of the contractor since the submission of the most recent written information dated 04/05/95 by the contractor to the Government in connection with the contract, that to the extent of any contract provision limiting progress payments pending first article approval, such provision has been complied with, and that after the making of the requested progress payment to unliquidated progress payments will not exceed the maximum unliquidated progress payments permitted by the contract.

Name and Title of Contractor Representative
 Signing This Form: Richard C. Vine, Director of Administration

Signature



Source: DOD

DFAS-COLUMBUS AUTOMATIC PAYMENT OF INVOICE

DFAS-Columbus uses the MOCAS API module to process payment requests. This method, implemented in 1982, is still in use today for approximately 80 percent of the progress payments processed by DFAS-Columbus. API distributes the payment to all available funds on the contract based on the weighted value of the total obligations for each ACRN. Progress payment distributions under API are done automatically after DFAS-Columbus personnel input information from hard copy progress payment requests. Steps taken to compute and distribute the progress payment are shown in table III.1.

Table III.1: API Progress Payment Distribution Procedures

Step	Step objective	Actions taken to accomplish step
1	Review each progress payment request and assign a batch number and Automated Data Processing Equipment (ADPE) number (internally generated tracking number).	Review progress payment request and assign ADPE number.

Step	Step objective	Actions taken to accomplish step
2	Enter in MOCAS the (1) contract number, (2) delivery order number, (3) "A" for U.S. funds or "B" for foreign military sales funds, (4) progress payment request number, (5) action code, (6) ADPE number, (7) contract dollar amount, (8) progress payment rate, (9) liquidation rate, (10) date of request, and (11) all information included on lines 9 through 27 of the progress payment request form (SF 1443) submitted by the contractor.	Review the progress payment request and enter required data. ^a
3	Calculate the amount of the progress payment to be distributed to each contract ACRN.	MOCAS API process computes the amount to be distributed and makes the distribution. ^b

^aFigure III.1 documents the data entered for the illustrative progress payment request.

^bFigure III.2 documents the distribution results for this illustrative progress payment request.

Source: GAO analysis based on DOD policies and regulations.

Figure III.2: MOCAS Generated Subvoucher

REPORT NUMBER MYEB 07 SUB-VOUCHER		CELL Y1	DATE 97 APR 16	PSSN 6356	DATE 04-16-97	VOUCHER NO. A663-72												
CHECK NO. 00592465	OR <input type="checkbox"/> CASH	AMOUNT OF PAYMENT 1,525,000.00																
PAID TO:		DATE																
SIGNATURE		AMOUNT																
CONTRACT OR OTHER AUTHORIZATION NUMBER	FT	DEPT	FY	ACCOUNTING CLASSIFICATION										AMOUNT				
				NAVY					AIR FORCE ARMY						ACCTG STA	BUD ACT USA		
				BU APP	OBJ	MPPR	BU CON	EXPEND ACCTG	FUND	LIMIT	OAC	SERIAL NUMBER	PROJ				SUB	OBJ
3	AA	21	52035	7J		55S	5S14	P532000								W	782,736.75	
3	AB	21	42035	JJ	028017	45S	5S14	P532000								W	742,263.25	
				25CZ	028017			BPRA010										
				25CZ	028017			BPRA010										
COLLECTIONS AND/OR DEDUCTIONS																		
* TYPE OF PAYMENT CODE	REMARKS																	
COMMERCIAL ACCOUNTS	CONTRACT TOTAL 1,525,000.00																	
1 COMPLETE OF FINAL	API																	
2 PARTIAL 033																		
3 WORK IN PROGRESS																		
4 ADVANCE																		
5 LAPSED FUND TRAVEL																		
6 ADVANCE																		
7 COMPLETE OR FINAL																		
8 PARTIAL																		

DLA FORM 1675 APR 81

REPLACES DD FORM 1524-1, 1 JUN 65, WHICH MAY BE USED UNTIL SUPPLY IS EXHAUSTED

FORM APPROVED BY COMPTROLLER GENERAL, U.S. 4 APR 56

Source: DOD

DFAS-COLUMBUS OCTOBER 3, 1995, POLICY MEMORANDUM

A DFAS-Columbus policy memo, which has been in effect since October 3, 1995, requires manual payments to be distributed to funds cited on the payment request or in accordance with contract terms. If specific payment instructions are lacking, payments are to be distributed in ACRN sequence based on alphabetic order, i.e., AA will always be first if used in contracts. This change in the manual payment distribution method was based on a September 28, 1995, memo issued by the DOD Comptroller. MOCAS' automatic process (API) did not change as a result of this memorandum. Steps taken to compute and distribute the progress payment are shown in table IV.1.

Table IV.1: DFAS-Columbus October 3, 1995, Policy Memorandum, Progress Payment Distribution

Step	Step objective	Actions taken to accomplish step
1	Determine contract specific pay instructions provided for in the contract.	Review the contract and payment request and determine if any specific payment instructions are provided. If provided, pay according to those instructions. If not provided, go to step 2.
2	Compute the amount of funds available from which to make this progress payment for each ACRN included in the contract.	Multiply the unliquidated obligation (ULO) balance by the progress payment rate and determine the maximum allowable amount for the work-in-process (WIP) line. Deduct the current WIP balance from the maximum allowable amount for the WIP line and determine the amount of funds available from which to make the progress payment.
3	Place contract ACRNs in alphabetic sequence.	Review the MOCAS contingent liability record to determine the ACRNs used on this contract. Rank the ACRNs in alphabetic sequence (AA will always be first).

Step	Step objective	Actions taken to accomplish step
4	Determine how much of the progress payment approved amount can be distributed to ACRNs on the contract.	Compare the amount of funds available on the first ACRN (computed in step 3) to the approved amount of the progress payment. Determine if the amount available to make the progress payment exceeds the amount of the approved progress payment. If yes, distribute the entire progress payment amount to the first ACRN. If no, distribute an amount equal to the maximum available amount to the next ACRN, and continue in this manner until the entire progress payment amount is distributed.

Source: GAO analysis based on DOD policies and regulations.

Applying the October 3, 1995, policy methodology to the illustrative progress payment request results in the following computations and appropriation distributions.

Table IV.2: Illustrative Example of Distribution Results Under October 3, 1995, Policy Memorandum

	Fiscal Year 1995 Other Procurement, Army	Fiscal Year 1994 Other Procurement, Army	Total
ULO balance	\$8,470,314.19	\$10,280,188.00	\$18,750,502.19
Multiplied by the progress payment rate	<u>.75</u>	<u>.75</u>	
Maximum WIP balance	\$6,352,735.64	\$7,710,141.00	\$14,062,876.64
Less current WIP balance	<u>2,721,585.58</u>	<u>4,267,197.54</u>	<u>6,988,783.12</u>
Available for WIP payment	\$3,631,150.06	\$3,442,943.46	\$7,074,093.52
Progress payment #10 distribution	\$1,525,000.00	\$0	\$1,525,000.00

Source: GAO analysis based on DOD policies and regulations.

DOD REGULATION 7000.14R, VOLUME 10 OTHER DISTRIBUTION

Volume 10 of DOD Regulation 7000.14R, issued on February 8, 1996, requires progress payments to be distributed based upon the distribution identified in the contract. When the contract does not cite specific payment instructions and only one military service is involved in the contract, the payment is to be prorated against those ACRNs with sufficient unliquidated obligations using the obligations as the basis of the proration. However, when the contract is funded with appropriations from multiple military services, the regulation requires that payment be distributed to the military services with sufficient unliquidated obligations and then to the ACRNs within that military service. Once again, the obligation will be the basis for the proration. In commenting on these examples, DFAS officials stated that using obligations as the basis when distributing progress payments is commonly referred to as the MOCAS API method. However, DFAS-Columbus personnel use other obligation based prorations. One such use of the regulation results in the steps shown in table V.1 being taken to compute and distribute the progress payment.

Table V.1: DOD Regulation 7000.14R, Progress Payment Distribution Procedures

Step	Step objective	Actions taken to accomplish step
1	Determine if any contract specific pay instructions are provided.	Review the contract and payment request and determine if any specific payment instructions are provided. If provided, pay according to those instructions. If not provided, go to step 2.
2	Determine which military services are funding the contract.	Review the funding for the contract and assess which military services have funds on the contract.
3	Compute, by ACRN, the amount of funds available from which to make this progress payment.	Multiply the ULO balance by the progress payment rate and determine the maximum allowable amount for the WIP line. Deduct the current WIP balance from the maximum allowable amount for the WIP line and determine the amount of funds available from which to make the progress payment .

Step	Step objective	Actions taken to accomplish step
4	Compute the distribution percentage for each ACRN on the contract.	Total the values computed in step 3 above to determine the total amount of funds available from which to make the progress payment. Divide each ACRN's funds available for progress payments by the total computed and determine the distribution percentage for each ACRN.
5	Compute how much of the progress payment approved amount can be distributed to each contract ACRN.	Multiply the approved progress payment amount by the percentage to be applied to each ACRN and determine the amount of the payment to distribute to each ACRN.

Source: GAO analysis based on DOD policies and regulations.

Applying this methodology to the illustrative progress payment request results in the following computations and appropriation distributions.

Table V.2: Illustrative Example of Other Distribution Results Under DOD Regulation 7000.14R

	Fiscal Year 1995 Other Procurement, Army	Fiscal Year 1994 Other Procurement, Army	Total
ULO balance	\$8,470,314.19	\$10,280,188.00	\$18,750,502.19
Multiplied by the progress payment rate	<u>.75</u>	<u>.75</u>	
Maximum WIP balance	\$6,352,735.64	\$7,710,141.00	\$14,062,876.64
Less current WIP balance	<u>2,721,585.58</u>	<u>4,267,197.54</u>	<u>6,988,783.12</u>
Available for WIP payment	\$3,631,150.06	\$3,442,943.46	\$7,074,093.52
Progress payment #10 distribution	\$782,782.50	\$742,217.50	\$1,525,000.00

Source: GAO analysis based on DOD policies and regulations.

AIR FORCE REGULATION 177-120

Air Force Regulation 177-120 required payments to be distributed to appropriations cited on the contractor-prepared payment request. Under this regulation, if the payment request did not cite specific funds, the oldest fiscal year funds were to be charged first using the following sequence of appropriation categories: (1) Air Force Research, Development, Test, and Evaluation (RDT&E)–Reimbursable Budget Authority (RBA) Budget Program Activity Code (BPAC), (2) Air Force RDT&E–Other Than RBA BPAC, (3) DOD RDT&E–Strategic Defense Initiative, (4) Air Force System Command Operation and Maintenance, (5) Air Force Procurement and Production appropriations, (6) Air Force Working Capital Funds (Industrial Fund and Stock Fund), (7) Air Force Operation and Maintenance–Other Major Commands, (8) all other funds, including Army, Navy, and DOD. According to DFAS officials, this regulation is no longer to be used as guidance when distributing progress payments. Steps taken to compute and distribute the progress payment under this regulation are shown in table VI.1.

Table VI.1: Air Force Regulation 177-120 Progress Payment Distribution Procedures

Step	Step objective	Actions taken to accomplish step
1	Determine if any contract specific pay instructions are provided.	Review the contract and payment request and determine if any specific payment instructions are provided. If provided, pay according to those instructions. If not provided, go to step 2.
2	Determine if any Air Force RDT&E or DOD Strategic Defense Initiative funds are available for the contract.	Review the funding for the contract and assess if any Air Force RDT&E or DOD Strategic Defense Initiatives are available.
3	Compute the amount of funds available from which to make this progress payment for each contract ACRN.	Multiply the ULO balance by the progress payment rate and determine the maximum allowable amount for each ACRN WIP line. Deduct the ACRN's current WIP balance from the ACRN's WIP line maximum allowable amount and determine the amount of funds available from which to make the progress payment.
4	Determine which ACRN represents the oldest fiscal year funds.	Review contract funding information and determine which ACRN represents the oldest fiscal year funds.

Table II.1, continued

Step	Step objective	Actions taken to accomplish step
5	Determine how much of the approved progress payment amount can be distributed to the oldest fiscal year funds.	Compare the amount of funds available for the oldest fiscal year appropriation (computed in step 3) to the approved amount of the progress payment. Determine if the amount available to make the progress payment exceeds the amount of the approved progress payment. If yes, distribute the entire progress payment amount to the ACRN. If no, distribute an amount equal to the maximum available amount to the oldest appropriations, and continue in this manner until the entire progress payment amount is distributed.

Source: GAO analysis based on DOD policies and regulations.

Applying the Air Force methodology to the illustrative progress payment request results in the following computations and appropriation distributions.

Table VI.2: Illustrative Example of Distribution Results Under Air Force Regulation 177-120

	Fiscal Year 1995 Other Procurement, Army	Fiscal Year 1994 Other Procurement, Army	Total
ULO balance	\$8,470,314.19	\$10,280,188.00	\$18,750,502.19
Multiplied by the progress payment rate	<u>.75</u>	<u>.75</u>	
Maximum WIP balance	\$6,352,735.64	\$7,710,141.00	\$14,062,876.64
Less current WIP balance	<u>2,721,585.58</u>	<u>4,267,197.54</u>	<u>6,988,783.12</u>
Available for WIP payment	\$3,631,150.06	\$3,442,943.46	\$7,074,093.52
Progress payment #10 distribution	\$0	\$1,525,000.00	\$1,525,000.00

Source: GAO analysis based on DOD policies and regulations

DFAS-COLUMBUS DESK PROCEDURE 302. MANUAL DISTRIBUTION

DFAS-Columbus Desk Procedure 302 was in effect from March 16, 1992, to October 3, 1995, and recognized that all payments should attempt to use the MOCAS API process. However, the procedure required that if MOCAS API could not be used, voucher examiners were to manually prepare the (1) Progress Payments Prorate Worksheets to determine if the progress payment could be made and the (2) Progress Payment Prorata forms to determine the amount of the progress payment to apply to each contract ACRN. This manual process attempts to mirror that used by the MOCAS API process. Steps taken to compute and distribute the progress payment are shown in table VII.1 and demonstrated in detail in figures VII.1 and VII.2.

Table VII.1: Desk Procedure 302. Manual Progress Payment Distribution Procedures

Step	Step objective	Actions taken to accomplish step
1	Enter MOCAS information pertaining to (1) contract number, (2) progress payment request number, (3) dollar amount of progress payment, (4) contract liquidation rate, (5) service code for each ACRN (1=Army, 2=Air Force, 3=DLA, and 4=Navy), (6) each ACRN, (7) obligation dollar amount for each ACRN, (8) WIP outstanding dollar amount for each ACRN, and (9) ULO balance dollar amount for each ACRN to the Progress Payments Prorate Worksheet.	Review MOCAS Contingent Liability Record and record the required information on the Progress Payments Prorate Worksheet. ^a

Step	Step objective	Actions taken to accomplish step
2	Determine and record on the Progress Payments Prorata Worksheet the amounts of funds available to make to the progress payment.	Multiply the ACRN ULO amount by the liquidation rate. Subtract each ACRN's WIP outstanding dollar amount from each answer computed and determine the available funds.
3	Sort ACRNs in ascending order based upon the dollar amount of funds available to make the progress payment.	Review the MOCAS contingent liability record to determine the ACRNs used on this contract. Rank the ACRNs in descending order and record the sequence of ACRNs on the Progress Payments Prorata Worksheet.
4	Record on the Progress Payment Prorata form from Progress Payments Prorata Worksheet the following information: (1) contract number, (2) progress payment request number, (3) service codes of ACRNs in ascending order, (4) each ACRN in ascending order, and (5) each ACRN's dollar amount of obligations.	Copy and record the required information to the Progress Payment Prorata form. ^b
5	Compute and record to the Progress Payment Prorata form the obligation balance for each ACRN on the contract.	Total the obligation dollar amounts recorded in column 3 and record the computed amount on column 4, line 1. Subtract column 3, line 1 from column 4, line 1 and enter this amount on column 4, line 2. Continue this process until column 3 and column 4 equal each other. ^b

Step	Step objective	Actions taken to accomplish step
6	Compute and record on the Progress Payment Prorata form the pro rate percent amount for each ACRN.	Divide each ACRN's obligation amount by each ACRN's obligation balance and determine the pro rate percent. Record the pro rate percent amount in column 5. ^b
7	Record on the Progress Payment Prorata form the dollar amount of funds available to make progress payment.	Review the Progress Payments Prorata Worksheet and enter the amounts in column 7 to column 6 on the Progress Payment Prorata form. ^b
8	Determine the dollar amount of the progress payment approved balance for the first ACRN listed on the Progress Payment Prorata form.	Review the progress payment request to determine the approved progress payment amount and enter this amount. ^b
9	Compute the amount of the progress payment to be prorated to the first ACRN listed on the Progress Payment Prorata form.	Multiply the approved balance in column 7, line 1 by the pro rate percent in column 5, line 1 to determine the amount to be prorated to the first ACRN. ^b
10	Determine the dollar amount of the progress payment approved balance for the second ACRN listed on the Progress Payment Prorata form.	Compare the amount of funds remaining to pay progress payments for the second ACRN to the amount of the prorated progress payment computed in step 9 and determine which is smaller. Record the smaller amount in column 8, line 1 of the Progress Payment Prorata form. Subtract the amount of the progress payment distributed to the first ACRN on the Progress Payment Prorata form from the progress payment approved balance on column 7, line 1 and record this amount in column 7, line 2. ^b

Step	Step objective	Actions taken to accomplish step
11	Determine the dollar amount of the progress payment approved balance for all remaining ACRNs on the contract.	Repeat steps 9 and 10 until columns 7, 8, and 9 are complete for all ACRNs. ^b

^aFigure VII.1 documents the data entered for the illustrative progress payment request

^bFigure VII.2 documents the information recorded for the illustrative progress payment request.

Source GAO analysis based on DOD policies and regulations.

Figure VII.1: Progress Payments Prorata Worksheet Example

PIIN/SPIIN								
PROGRESS PAYMENTS PRORATA WORKSHEET								
MULTI ACRNS-ONE SERVICE	MULTI ACRNS - MULTI SERVICE				MULTI ACRNS - FMS			
	1	2	3	4	5	6	7	
PPR	SVC/CC	ACRN	OBLIGATION	WIP O/S	ULO	AVAIL FUNDS	ACRN/SVC ASCEND ORDER	
APPROVED	1	AA	\$14,652,354 07	\$2,721,585.58	\$3,470 914 19	\$3 631,150 06	AA	\$3,631,150 06
	1	AB	13 894,788 00	4,267,197 54	10,280 188 00	3 442,943 46	AB	3 442 943 46
LIO RATE								
CC DISTRIBUTION								
TOTAL FUNDS AVAILABLE								

Source: GAO analysis based on DOD policies and regulations.

Figure VII.2: Progress Payment Prorata Form Example

PIIN/SPIIN									
PROGRESS PAYMENT PRORATA									
									PPR
1	2	3	4	5	6	7	8	9	
SVC/CC	ACRN	OBLIGATION	OBLIGATION BALANCE	PRO RATE PER CENT	FUNDS REMAINING TO PAY PROGRESS PAYMENT	PROGRESS PAYMENT APPROVED BALANCE	PRO RATED PROGRESS PAYMENT	AMOUNT CHARGED TO SERVICE / ACRN	
1	AA	\$14,652 354 07	\$28 547,142 07	0 51327	\$3 631 150 06	\$1 525 000 00	\$782 736 73		
1	AB	13,894,788 00	13,894,788 00	1	3,442,943 46	742,263.25	742,263.25		

Source: GAO analysis based on DOD policies and regulations.

COMMENTS FROM THE DEPARTMENT OF DEFENSE

COMPTROLLER

UNDER SECRETARY OF DEFENSE
1100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100



JUN 27 1997

Mr. Gene L. Dodaro
Assistant Comptroller General
Accounting and Information Management Division
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Dodaro:

This is the Department of Defense response to the General Accounting Office (GAO) draft report, "FINANCIAL MANAGEMENT: DoD Progress Payment Distribution Procedures," dated June 6, 1997 (GAO Code 918912/OSD Case 1380).

The Department appreciates the changes made to the original draft concerning the procedures utilized in making progress payments. However, the chart on page 4 and some of the associated language might lead the reader to conclude that the Department follows more policies than one. For the record, I want to make the following points:

The Defense Finance and Accounting Service (DFAS) pays all progress payments in a manner stipulated in contracts or as directed by special payment instructions from contracting officers. The DFAS uses the payment procedures discussed below only if there are no specific contract payment provisions or instructions. The DFAS Columbus Center has only one overall policy that governs how progress payments are made, supplemented by a policy memorandum that is used when payments fail the Automatic Payment of Invoices (API) process.

The DoD Financial Management Regulation (DoD FMR) 7000.14R, issued February 1996, is the governing policy that provides standard distribution guidelines for the allocation of progress payments. The DoD FMR replaces payment guidance previously existing under various DoD regulations, orders, or policies. The DoD FMR currently allows for two methods of distribution: (1) specific itemization as requested and directed in the contract or (2) proration using obligation balances (commonly referred to as the API method). Only one method is used on an invoice per contract. Also, the DFAS Columbus Center issued an intensive policy memorandum on October 3, 1995, which delineates procedures to distribute manual progress payments based on a directive prescribed by the DoD Comptroller in a September 28, 1995, memorandum.

A further elaboration of the FMR's two methods is as follows:

- Contract Specific Instruction. The DoD FMR requires payment allocation in accordance with instructions provided within the individual contracts. Often, due to the potential for canceling funds under Public Law 101-510, contract specific instructions similar to those contained in

the now expired Air Force Regulation 177-120, Accounting and Finance Central Procurement Transactions, are contained in selected contracts. These instructions may require payment distribution to the oldest fiscal year funds first. This method is used approximately 15 percent of the time.

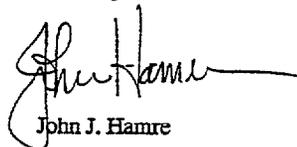
- Automatic Payment of Invoices (API). If no specific instructions are included in the contract, the FMR requires payment based upon the API process. This process establishes a payment distribution procedure that uses the weighted value of the contract's obligation balances to determine payment distribution. This automated method is in use today for approximately 80 percent of the progress payments processed by the DFAS Columbus Center.

Also, as noted above, this overall policy is supplemented by an October 3, 1995, DFAS Columbus policy memorandum. The memorandum prescribes payment distribution in "ACRN alphabetic order" when specific payment allocation instructions were not provided in the contract, when payments are not systemically entitled via the API process, or when a request for authorization to pay is denied during the prevalidation process. This guidance was initiated due to insignificant dollar amounts being allocated by the API process which degraded payment timeliness when payments were subjected to the prevalidation process.

I will issue, shortly, guidance requiring the contracting officer or contract administration office to provide DFAS specific instructions on how to distribute each progress payment. The distributions are to reflect the contract line item level costs incurred by the contractor. These distributions will be required for all progress payments requested under new contracts.

When discussing progress payments, it is important that they be distinguished from delivery payments. Progress payments are contract financing payments that are applicable only to fixed price contracts. Progress payments do not represent payments for work or services that have been completed or delivered. Progress payments represent financing to contractors based on costs incurred and the contractor remains liable for the financing until the items specified in the contract are delivered. The use of progress payments on large contracts is authorized by law for all Federal Agencies because this process produces the lowest overall cost to the government. Contractors pay higher interest rates than the Treasury and those interest rates would be included in contract prices. When the contractor delivers the items or services specified in the contract, the applicable outstanding progress payments amount is deducted from the price of the delivered items before the payment is made.

Sincerely,



John J. Hamre

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